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Early Converts Rethink OCIO Model

By Aziza Kasumov
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Outsourced CIOs (OCIOs) are still raking in new assets, but a growing number of investors are turning back to non-discretionary consultants as the first generation of OCIO adopters' contracts come up for bid.

After 10 years of rallying stock markets and disappointing results in alternatives, it's "not uncommon" to see some asset owners go against the industry trend and quit outsourcing, some search consultants say.

The **Ohio University Foundation,** for example, is doing exactly this.

The university had used Hirtle Callaghan's OCIO services since 2009, according to a trustee meeting summary. But, at the beginning of the year, the endowment issued a request for proposal for a more "collaborative, non-discretionary based" consultant, *FundFire*'s sister publication *MandateWire* reported.

The university expects to announce the final decision on the search by June 30, **David Gaume**, the school's director of investments, writes in an email.

Since hiring Hirtle Callaghan as its OCIO in 2009, the endowment grew from $253 million to $536 million as of the end of 2017, according to the school's annual report.

That "significant growth of assets under management over the last decade" prompted the foundation's investment committee to take a closer look at its investment management set-up to see whether it was still a good fit, Gaume writes.

Gaume says the foundation's investment committee began reviewing its OCIO relationship last fall. By then, the portfolio, under Hirtle Callaghan's management, had also started missing its benchmark and lagging its peer group. Year-to-date returns by June 30, 2018, were -0.8%, one-year returns at 6.5%, according to a investment committee call summary from August. Even before then, at the end of 2017, the endowment's three-year return rate was 1.6 percentage points lower than its peer group average, according to the school's annual report. The five- and ten-year-return rates were also lower, the report said.

A spokeswoman for Hirtle Callaghan could not be reached for comment by publication deadline.

"After a 10-year bull market, your assets are bigger, and you might just insource," says **Anna Dunn Tabke**, principal at Alpha Capital Management, which provides OCIO search services to institutional investors. That "break-event point, above which it makes sense to run things in-house," is getting close to $500 million to $1 billion, says **Chris Cutler**, founder of investment consulting firm **Manager Analysis Services.**

That's exactly the asset size range Ohio University entered in the past few years – and the school isn't the only institution that has chosen to take things back in-house at that point. In 2016, **Howard University** also exchanged its OCIO for an internal investment office supported by some outside consultants. The school's endowment had a market value of roughly $577 million around then, according to the school's annual report.

Now, with a wave of early OCIO adopters going back to market to check for better options, as reported, some consultants are saying more institutions may consider a move away from outsourcing.

"We definitely see it in those 'gen-two searches'," says Tabke. She adds that she's seen one client abandon its OCIO provider and hire in-house staff, and three to four additional clients consider such a move. "People have been with OCIOs long enough to start drawing conclusions," Cutler says.

There are other reasons why institutions might take investment operations back in house.

With performance in hedge funds and alternatives not being as great as it used to be, "you find situations where… you have boards [at smaller institutions] that are finding that their liquid strategies are doing quite well," Cutler says. In those cases, "Why would they outsource? They can just do it themselves," he adds. Additionally, insourcing allows for more tailored services. "A lot of OCIOs are focused on performance, not necessarily on institutional cash flow needs," Cutler says.

The business cycle, Tabke says, can play a role, too. OCIO fees are compressing, but they're still higher than those for non-discretionary advisory services. "Just about everyone is expecting lower returns going forward, so it can be a good time to do a gut check," she says.

Ultimately, though, "it's always going to come back to performance," Tabke says.